Before the
Federal Communications Commission
Washington, DC 20554

In the matter of	)	
	)	
Federal-State Joint Board on Universal Service	)	CC Docket No. 96-45
	)	
	)	

To: The Federal-State Joint Board

REPLY COMMENTS OF
RURAL CELLULAR ASSOCIATION
AND
<u>THE ALLIANCE OF RURAL CMRS CARRIERS</u>

David A. LaFuria
David L. Nace
Steven M. Chernoff
Lukas, Nace, Gutierrez & Sachs, Chartered
1650 Tysons Blvd., Suite 1500
McLean, VA 22102
703-584-8678

December 14, 2004

Summary

The comments submitted in response to the Joint Board's Public Notice expressed a wide range of views, but one theme was constant: universal service support mechanisms must promote efficient investment. RCA-ARC agrees strongly with several commenters that the FCC's decision to make "portable" per-line support available to competitive eligible telecommunications carriers ("CETCs") is competitively neutral, creates appropriate incentives, and has yielded enormous benefits in rural areas where wireless CETCs have been designated.

RCA-ARC members have been designated in several states and are investing high-cost support in facilities and services to consumers in areas in need of a reliable alternative to wireline service. The per-line support mechanism works because it requires CETCs to invest in an area based upon sound market-based principles, not upon the carrier's desire to be "made whole." Any decision to pay CETCs based on recovery of their own costs would encourage inefficient investment. More importantly, given the longstanding (and increasing) over-subsidization of rural ILECs, it would do nothing to control the growth of the high-cost fund.

For similar reasons, rural ILECs should be transitioned to receiving support based on forward-looking economic cost. The current embedded-cost system provides no incentives for ILECs to reduce costs, and the result thus far is a proliferation of high dividend payouts and inefficient investment plans. A forward-looking methodology will accomplish one critical objective – eliminating the incentive for ILECs to make inefficient investments in order to garner support. RCA-ARC urges serious consideration of the interim and long-term forward-looking cost solutions proposed by other commenters representing the wireless industry.

The Joint Board and the Commission have properly declined ILECs' invitation to target CETCs without addressing broader concerns about support paid to rural carriers. It has been

eight years since Congress declared that all telecommunications markets should be opened to competition, and seven years since the Commission announced its intent to move rural wireline companies to forward-looking costs. Rural consumers have benefited from the efficient investment that competitive per-line support provides, and they will benefit even more when rural ILECs are given similar incentives.

RCA-ARC therefore urges the Joint Board and the Commission to retain the invaluable per-line support mechanism for CETCs, and to promptly select a forward-looking cost methodology for rural ILECs so that it may be implemented as close to June of 2006 as possible.

Table of Contents

Before the
Federal Communications Commission
Washington, DC 20554

In the matter of	)	
	)	
Federal-State Joint Board on Universal Service	)	CC Docket No. 96-45
	)	
	)	

To: The Federal-State Joint Board

REPLY COMMENTS OF
RURAL CELLULAR ASSOCIATION
AND
THE ALLIANCE OF RURAL CMRS CARRIERS

Rural Cellular Association[1] ("RCA") and the Alliance of Rural CMRS Carriers[2] ("ARC") (collectively, "RCA-ARC"), by counsel and pursuant to the Commission's Public Notice, "Federal-State Joint Board on Universal Service Seeks Comment on Certain of the Commission's Rules Relating to High-Cost Universal Service Support," 19 FCC Rcd 16083 (Jt. Bd. 2004) ("*Public Notice*"), hereby provides the following reply comments.

I. INTRODUCTION

RCA-ARC members provide commercial mobile services in many rural areas throughout the U.S. They have collectively petitioned and obtained grants of eligible telecommunications carrier ("ETC") status in 16 states and the territories of Guam and Saipan, and as such are well

---

1 RCA is an association representing the interests of more than 100 small and rural wireless licensees providing commercial services to subscribers throughout the nation. Its member companies provide service in more than 150 rural and small metropolitan markets where more than 15 million people reside.

2 ARC is a group of CMRS carriers who are licensed to serve rural areas in Alaska, Colorado, Guam, Iowa, Kansas, Maine, Michigan, Minnesota, Nebraska, New Hampshire, Oklahoma, Oregon, Vermont, Virginia, Washington, West Virginia and Wisconsin. ARC's membership is comprised of the following carriers (or their subsidiaries): Alaska DigiTel, LLC, Cellular South Licenses, Inc., Guam Cellular and Paging, Inc., Highland Cellular, Inc., Midwest Wireless Communications, LLC, N.E. Colorado Cellular, Inc., Rural Cellular Corporation, RFB Cellular, Inc., and Virginia Cellular, Inc.

versed in the ETC designation process and in carrying out their respective obligations as competitive ETCs ("CETCs"). RCA-ARC members are today using high-cost support to further Congress' twin goals of advancing universal service and introducing competition to rural areas. The FCC has to date provided exactly the correct incentives for rural CMRS carriers to obtain ETC status and improve this nation's critical wireless infrastructure. As carriers who serve almost exclusively in rural areas, RCA-ARC is qualified to provide the Joint Board with commentary on the questions raised in the above-referenced Public Notice.

II. RURAL AMERICA IS CRYING OUT FOR IMPROVED WIRELESS SERVICE QUANTITY AND QUALITY

As RCA-ARC members have applied for ETC status in many states, they have experienced one consistent theme: Rural America wants wireless telecommunications services that are comparable to those in urban areas. This is no small matter. Wireless communications services are critical to health and economic development in rural areas. For example, the Maine Sheriffs Association recently passed a resolution supporting prompt FCC action on service area redefinition because it believes wireless service must be improved in Maine.[3] In Nebraska, literally dozens of consumers wrote letters to an RCA and ARC member who was just recently licensed to serve the western half of the state, describing the poor state of wireless services in small rural communities.

ARC members and undersigned counsel have met with dozens of state public utility commissioners, and members of the U.S. Congress, virtually all of whom describe receiving complaints from consumers about the number of wireless carriers actually providing services beyond big cities and major roads. RCA-ARC members' experience belies OPASTCO's contention that CMRS providers "have been successfully serving rural markets for many years

[3] A copy of the resolution is attached hereto as Exhibit A.

now without any high-cost funding."[4] OPASTCO selectively refers to a portion of the *Ninth CMRS Competition Report* stating that counties with fewer than 100 persons per square mile have an average of 3.9 wireless competitors.[5] This statistic is misleading because, in rural America, oftentimes there are multiple wireless carriers with *some* facilities in a county seat or primary town, which is a population center and usually located near a major road. But beyond the main town or major roadways, service is often limited to one carrier, or no carrier. In such areas, additional cell sites must be constructed to improve service quality. Tellingly, OPASTCO ignores the critical finding that counties in which three or more wireless carriers provide service constitute only 62% of the nation's land area.[6] The remaining 38% of the country is precisely where Congress intended for universal service to drive infrastructure investment so that consumers can have the benefit of the kinds of telecommunications services available in urban areas.

III. THE STATED PURPOSE OF UNIVERSAL SERVICE AS MANDATED BY CONGRESS MUST BE FAITHFULLY HONORED

When the 1996 Act was enacted, telephone penetration in the U.S. was 95% nationwide.[7] Without question, the overarching goal of connecting subscribers to the network had been reached. Yet Congress included in the 1996 Act specific provisions to permit competitive carriers to become ETCs.[8] Congress' goal, to remove implicit high-cost support so as to level the

---

4 OPASTCO Comments at p. 14.

5 *Implementation of Section 6002(b) of the Omnibus Budget Reconciliation Act of 1993, Annual Report and Analysis of Competitive Market Conditions With Respect to Commercial Mobile Services,* CC Docket No. 04-111, *Ninth Report,* FCC 04-216 (rel. Sept. 28, 2004) ("*Ninth CMRS Competition Report*"), ¶ 109.

6 *See id.* at ¶ 49.

7 Telephone Subscribership in the United States – Data Through November 1996 (rel. Jan. 1997) at p. 18, Table 3. See http://www.fcc.gov/Bureaus/Common_Carrier/Reports/FCC-State_Link/IAD/subs1196.pdf.

8 *See* 47 U.S.C. Sections 214, 254.

playing field for all carriers, could not have been more clear. The entire purpose of the 1996 Act was pro-competition and deregulatory.[9]

Nowhere in the 1996 Act or its legislative history did Congress state that its goal for universal service going forward was to consign any part of rural America to a single monopoly carrier, providing only one technology, subsidized by users of other more efficient or desirable technologies. Far from choosing a preferred technology, Congress directed the FCC to use universal service to provide rural consumers with access *to the same kinds of telecommunications choices and at similar rates* available to those in urban areas, consistent with the Act's core mission to promote competition and deregulate telecommunications.[10]

When incumbents challenged the FCC's interpretation of the 1996 Act and its implementation, the Fifth Circuit adamantly upheld the Commission:

> Petitioners' various challenges fail because they fundamentally misunderstand a primary purpose of the Communications Act--to herald and realize a new era of competition in the market for local telephone service while continuing to pursue the goal of universal service. They therefore confuse the requirement of sufficient support for universal service within a market in which telephone service providers compete for customers, which federal law mandates, with a guarantee of economic success for all providers, a guarantee that conflicts with competition.[11]

To date, the FCC and the Courts have consistently upheld the fundamental purpose of the 1996 Act that Congress enacted – to remove support from ILEC rate structures, to open access to

---

[9] "An Act to promote competition and reduce regulation in order to secure lower prices and higher quality services for American telecommunications consumers and encourage the rapid deployment of new telecommunications technologies." Telecommunications Act of 1996, Pub. L. No. 104-104, preamble, 110 Stat. 56.

[10] 47 U.S.C. Section 254(b)(3).

[11] *Alenco Communications, Inc. v. FCC*, 201 F.3d 608, 625 (5^{th} Cir. 2000).

support by competing carriers, and to drive infrastructure investment to provide higher quality competitive services to rural Americans at the earliest possible date.[12]

RCA-ARC members operate almost exclusively in rural areas. They face exactly the same challenges as those faced by ILECs and identified by the Rural Task Force in its White Paper No. 2.[13] But rural wireless carriers are not on a level playing field with incumbent carriers, who operate under rate of return regulation and a modified embedded cost methodology for calculating support that guarantees a profitable business, while permitting many, if not most, to charge artificially low rates for access to the public switched network. Incumbents also have complete control of the local exchange marketplace.[14]

Some have argued that current federal policy may foster "artificial competition," that is, supporting multiple networks in areas that cannot support even one. Generally, this view is espoused by monopolists and is diametrically opposed to the Act's command to advance universal service in high-cost areas. We can find nowhere in the 1996 Act or its legislative history any expression that the new law was intended to support a single network. Far from it – the FCC has reached precisely the opposite conclusion.[15] Most rural Americans, who literally cry

---

12 *See Implementation of the Local Competition Provisions in the Telecommunications Act of 1966, First Report and Order,* 11 FCC Rcd 15499, 15506 (1996) ("*Local Competition Order*") ("The opening of all telecommunications markets to all providers will blur traditional industry distinctions and bring new packages of services, lower prices and increased innovation to American consumers. The world envisioned by the 1996 Act is one in which all providers will have new competitive opportunities as well as new competitive challenges.")

13 *See generally* "The Rural Difference," RTF White Paper #2 at pp. 15-30.

14 Investment industry analysis consistently values rural ILEC businesses higher than RBOCs because of favorable regulatory treatment and higher barriers to entry.

15 *See Federal-State Joint Board on Universal Service, Report and Order,* 12 FCC Rcd 8776, 8802 (1997) ("*First Report and Order*") ("Our decisions here are intended to minimize departures from competitive neutrality, so as to facilitate a market-based process whereby each user comes to be served by the most efficient technology and carrier. We conclude that competitively neutral rules will ensure that such disparities are minimized so that no entity receives an unfair competitive advantage that may skew the marketplace or inhibit competition by limiting the available quantity of services or restricting the entry of potential service providers.").

out for improved wireless services and competition for their local exchange carrier, would revolt at such a notion. What is artificial is providing support to a monopoly carrier and, by regulatory fiat, locking out competitors who are ready, willing and able to deliver services that consumers in rural areas are demanding.

Restricting access to the fund by competitive carriers in order to control growth of the fund is a solution to a problem that simply does not exist. Controlling growth of the fund is a burden to be shared by all carriers to be sure. However, the place to begin is the Schools and Libraries program and examination of increases in high-cost support paid to rural ILECs. Without portability, artificial monopolies are perpetuated.

In examining state universal service mechanisms that would thwart the 1996 Act's purposes, the FCC has unequivocally ruled that a competitive carrier cannot be expected to enter a market where an incumbent has all the customers and all the support.

> A new entrant faces a substantial barrier to entry if its main competitor is receiving substantial support from the state government that is not available to the new entrant. A mechanism that makes only ILECs eligible for explicit support would effectively lower the price of ILEC-provided service relative to competitor-provided service by an amount equivalent to the amount of the support provided to ILECs that was not available to their competitors. Thus, non-ILECs would be left with two choices -- match the ILEC's price charged to the customer, even if it means serving the customer at a loss, or offer the service to the customer at a less attractive price based on the unsubsidized cost of providing such service. A mechanism that provides support to ILECs while denying funds to eligible prospective competitors thus may give customers a strong incentive to choose service from ILECs rather than competitors. Further, we believe that it is unreasonable to expect an unsupported carrier to enter a high-cost market and provide a service that its competitor already provides at a substantially supported price. In fact, such a carrier may be unable to secure financing or finalize business plans due to uncertainty surrounding its state government- imposed competitive disadvantage. Consequently, such a program may well have the effect of prohibiting such competitors from providing telecommunications service, in violation of section 253(a).[16]

[16] *Western Wireless Corporation Petition For Preemption Of Statutes And Rules Regarding The Kansas State Universal Service Fund Pursuant To Section 253 Of The Communications Act Of 1934, Memorandum Opinion & Order*, 15 FCC Rcd 16227, 16231 (2000) (footnote omitted) ("*Kansas Preemption Order*").

All but a few states have flatly rejected the incumbents' world view of universal service – that it is a set-aside program for ILECs, with support intended solely to connect subscribers to the telephone network and subsidize existing ILEC operations. RCA-ARC members have been successful in obtaining ETC status because they have consistently advocated positions that embrace the law that Congress wrote and have only asked for treatment that is consistent with the Act.

As envisioned by Congress, RCA-ARC members have rapidly accelerated the deployment of telecommunications infrastructure in every area where they have been designated. ARC members have submitted ex parte presentations in this Docket to place into the record evidence of their use of funds to benefit rural communities. Rural consumers are seeing improved wireless service, many more areas where 911 and E-911 services are available, economic development opportunities, and the advancement of mobile wireless technologies that have been available in urban areas since the mid-1980s.

This success has not come without a steep price. Throughout the past six years, incumbent carriers have expended enormous effort to thwart RCA-ARC members from receiving grants of ETC status across America so as to promote inter-modal competition. It is not an exaggeration to state that oppositions have significantly delayed the competitive entry that Congress intended to occur, to the substantial detriment of rural consumers. Capital that could have been spent on networks has gone to litigation. Support that should have been readily available has been tied up in service area redefinition proceedings, in some cases for as long as two years.[17]

---

[17] *See* Public Notice, DA 03- 26, *Pleading Cycle Established For Comments On Proceeding Regarding The Definition Of The Rural Service Areas Of Two Rural Telephone Companies In The State Of Colorado,* CC Docket No. 96-45 (Jan. 7, 2003).

RCA-ARC urges the Commission to uphold the law Congress wrote and the many decisions it has rendered to date in implementing the 1996 Act. CETCs are only beginning to deliver the benefits that Congress promised and this proceeding will likely determine whether rural America will continue to see rapid deployment of critical wireless infrastructure that is so vitally needed.

IV. THE CURRENT PER-LINE METHODOLOGY LIMITS FUND GROWTH WHILE FORCING COMPETITORS TO INVEST IN RURAL AREAS IN ORDER TO GAIN SUPPORT

On May 5, 2003, RCA-ARC submitted comments in this docket, including commentary from Don J. Wood detailing why the current per-line methodology provides appropriate market signals to all participants. Mr. Wood explained that the current rules for providing high-cost support do not create an advantage for the CETC.[18] Mr. Wood explained that if a CETC's costs are higher, whether because it operates inefficiently, uses a less efficient technology for the area in question, or both, a CETC that receives support based on the incumbent's costs will not find it financially viable to enter the geographic market and invest in facilities. This is the desired result: a less efficient provider should not be encouraged to enter, nor should its entry be supported. However, when a CETC's costs are equal to or lower than the IETC's, then it is likely to enter and should be encouraged to do so. Competitive entry by a lower-cost carrier will inure to the consumer and reduce the need for high-cost support in the long run.

During the transition period during which competitive networks are being constructed, the incumbent's costs are the appropriate benchmark. Once competitive networks are constructed, the better benchmark is the lower-cost provider, which encourages efficiency and sends the correct signal to the marketplace. If a CETC's costs are lower than an incumbent's, it

---

[18] *See* RCA-ARC Comments in CC Docket No. 96-45 (filed May 5, 2003) at Exhibit 1, "Effective Long-Run Management of the High-Cost Universal Service Support Mechanism."

will force the incumbent to become more efficient. If an incumbent refuses to do so during the transition period, it may be unable to retain its ETC status or remain in business long term. This is a natural consequence of competitive markets and Congress has not guaranteed rural ILEC survival. In reality, rural ILECs are well positioned to improve efficiencies, exploit the natural advantages of a wireline network for data, and use wireless technologies to compete with newcomers.

Some commenters wrongly claim that use of the ILEC's per-line support level is a "windfall" for CETCs. In fact, since CETCs must use all available support for the provision of facilities and services,[19] there can be no windfall. Any so-called excess support results in competitive networks being constructed at an accelerated pace. Moreover, since most every newcomer has a much younger network than the incumbent, there are normally very substantial construction projects that must be undertaken to construct and upgrade networks that are capable of competing with incumbents *throughout the service area.*

For example, Midwest Wireless Communications, LLC ("Midwest") and Rural Cellular Corporation ("RCC") cover substantially all of the rural areas in the state of Minnesota. Collectively, their annualized projected support amount is approximately $28 million.[20] The annualized projected high-cost support amount for ILECs serving the same area is close to $85 million.[21] With few exceptions, this pattern is repeated throughout the country.[22] Midwest and RCC are expected to respond to all reasonable requests for service with far less available support

---

19 47 U.S.C. Section 254(e); 47 C.F.R. Section 54.7.

20 Source: www.universalservice.org, First Quarter Appendices - 2005 at HC01.

21 *Id.*

22 In Vermont, RCC, an ETC throughout the entire state, is projected to receive roughly $6.5 million in support in 2005. ILECs in Vermont serving the same area are projected to receive roughly $28 million. (See, http://www.universalservice.org/overview/filings/2005/Q1/default.asp at HC01.

than ILECs. Moreover, no matter how many ETCs are designated in these areas, fund growth is effectively capped because there is a finite number of customers and lines available to competitors.

Some have argued that wireless carriers are receiving support for existing customers that were acquired under business plans that did not anticipate universal service support and therefore support should not be paid on existing lines.[23] This argument evidences a fundamental misunderstanding of how the system is intended to work. First, any rational carrier not receiving support is going to begin to construct its network in areas expected to produce profits for the carrier. Any high-cost support that is later received for customer lines in those areas would be used to construct networks outward into other high-cost areas. Second, if the areas where a rational carrier has constructed are in fact low-cost, then the ILEC has a responsibility to disaggregate support so that uneconomic support levels are not distributed to CETCs. Disaggregation will drive higher per-line support amounts out to higher cost areas, so that CETCs have an appropriate incentive to construct facilities in these areas to the benefit of consumers who need them most.

V. PAYING EACH CARRIER ON ITS OWN COSTS WILL DRAMATICALLY INCREASE FUND GROWTH

Any method for providing high-cost support based on the CETC's costs would presumably ensure that the competitor could earn a sufficient return on investment. In such a case, it is possible, if not likely, that inefficient investments would be made by CETCs based on the ability to get high-cost support, irrespective of whether a business case can be made for competitive entry. In RCA-ARC's view, this is exactly the wrong result. Today, a CETC can

---

[23] *See* OPASTCO Comments at p. 14.

only get support if the potential customer revenue and support available are sufficient to permit competitive entry – that is, CETCs have the proper market entry information to determine whether to risk making the commitments necessary to become a CETC.[24]

ILECs who argue for support to be paid on a CETC's costs presume that the competitor has a lower cost structure and would presumably require less support. These presumptions may be incorrect and if the wrong choice is made, the fund size is likely to expand rapidly. First, any cost model developed for a competitor's technology must necessarily include the cost of constructing an entire network in the ETC service area, not just the existing network. Second, because in almost every case the CETC has far fewer lines than an incumbent, its per-line costs are likely to be far higher.

VI. THE CURRENT METHODOLOGY FOR PROVIDING SUPPORT TO ILECS IS INEFFICIENT

CenturyTel boasts that when it acquires smaller ILEC networks, it routinely spends tens of millions to improve networks "long neglected" and in "disrepair."[25] If true, this completely undercuts ILEC claims that modified embedded costs and rate of return regulation encourage investment and that incumbents are efficient.

Recently, USA Today published an article highlighting that some rural ILECs are paying out to their shareholders an annual dividend that exceeds what the shareholders pay for telephone service.[26] In 2004, Citizens Telecommunications paid out a special dividend of $300 million to its shareholders. It took in approximately $110 million in high-cost support. Given the

---

24 Of course, where support for ILECs is disaggregated, support is more accurately targeted to high-cost areas.

25 CenturyTel Comments at p. 19.

26 *See* "Fees Paid by All Phone Customers Help Rural Phone Firms Prosper," USA Today (11/16/2004), at http://www.usatoday.com/money/industries/telecom/2004-11-15-rural-phone-fees x.htm.

company's federally-funded magnanimity, Citizens' admonition that "[u]niversal service funding is not designed to subsidize companies; it is designed to protect and advance the interests of rural consumers"[27] must be taken *cum grano salis*. Plainly, this system is not forcing carriers to be accountable.

Many carriers claim that high-cost support is reimbursement for actual costs. Yet the vast majority of rural carriers do not submit cost data to NECA in order to qualify for support, but receive support pursuant to an "average schedule" methodology that requires no information on actual costs. In the recent *en banc* hearing, the Joint Board heard that USAC audits only approximately one ILEC per year. With over 1300 rural carriers, each one will have been audited by sometime around the year 3304 at the current pace.

Nobody knows the actual costs of operation of most rural ILECs and nobody knows whether they are being over- or under-compensated. The current modified embedded cost system does not produce cost data open to analysis and there is evidence that suggests it encourages inefficient investment. For example, the Helix Telephone Company in Oregon serves approximately 500 access lines in two non-contiguous wire centers. Helix applied to the Oregon Public Utility Commission ("OPUC") for a waiver of local number portability ("LNP") requirements because it would be unduly burdensome to replace both of their switches, each at a cost of over $250,000.[28] With the availability of soft switches, switch sharing capabilities, and other possible solutions, it is inconceivable that any carrier would invest in two switches amounting to $500,000 to upgrade 500 access lines *if it were in a competitive marketplace*.

---

27 Frontier/Citizens Comments at p. 6.

28 Helix Telephone Co., Petition for Suspension of Wireline to Wireless Number Portability Obligations, Docket No. UM 1125 at p. 2 (Or. PUC, Jan. 27, 2004) ("Helix Order").

Another network design almost certainly could provide a more efficient means to offer LNP, but Helix has no incentive to facilitate a choice of service providers for consumers.

In Colorado, PC Telecom claimed that it could not provide LNP because it has not upgraded its equipment in many years. In the course of the proceeding, it was discovered that its subscribers do not yet have “CLASS features,” such as caller ID and call waiting, some 20 years after they were introduced in this country. From ARC member N.E. Colorado Cellular’s (“NECC”) perspective, embedded costs have only permitted PC Telecom to collect support with no obligation to improve its network. In the meantime, it has vigorously opposed NECC’s ETC petition and asked for an eighteen month extension of the LNP requirement.

ILECs consistently claim that the modified embedded cost methodology provides appropriate incentives for carriers to invest in their networks and a move to forward-looking costs will dampen such incentives. Yet they have provided almost no evidentiary data to support these claims. Examples of high dividend payouts, inefficient investment plans, and poor facilities, are not difficult to find. Surely there are areas where rural consumers have first rate wireline facilities, however universal service support was intended to ensure that all areas have first rate service and that consumers have a choice in service providers. Wireless carriers seek funds to extend service and compete for consumers who have few or no choices in wireless services. Congress understood full well that competition for support and consumers is the only practical way to encourage efficiencies and innovation from all carriers, to the benefit of rural consumers.

VII. IN ORDER TO LIMIT FUND GROWTH, THE COMMISSION MUST MOVE RURAL CARRIERS TO FORWARD-LOOKING COSTS

Of all the myths perpetuated by rural ILEC lobbyists, perhaps the most egregious is the contention that CETCs are the “main” cause of growth in the fund. It is becoming clear that this myth, too, is falling away, as even ILECs are beginning to acknowledge that a major factor in fund growth is excessive support to rural telephone companies.[29] If total support to incumbent and CETCs in rural areas is excessive, then attention must be focused on the companies on whose costs such support is based; indeed, high-cost funding to rural ILECs was excessive long before CETCs appeared on the scene. Moreover, while the chart on p. 8 of NTCA's comments purports to show the predictable and fully anticipated increase in support to newly designated competitors that are aggressively investing in infrastructure, the same chart shows a 5% increase in support to rural ILECs, whose networks are fully matured. NTCA fails to explain this increase and whether there were any attendant benefits to consumers.

In 1996, the Joint Board recommended basing support for all carriers on a forward-looking cost system. The FCC adopted the Joint Board's recommendation in 1997. A review of the First Report & Order reveals that the Commission carefully considered and unequivocally adopted forward-looking costs as the preferred method for preserving universal service:

> We agree with the Joint Board and many commenters that, in the long run, forward-looking economic cost best approximates the costs that would be incurred by an efficient carrier in the market. We concur with the Joint Board's finding that the use of forward-looking economic costs as the basis for determining support will send the correct signals for entry, investment, and innovation.
>
> We agree with the Joint Board that the use of forward-looking economic cost will lead to support mechanisms that will ensure that universal service support corresponds to the cost of providing the supported services, and thus, will preserve and advance universal service and encourage efficiency because support levels will be based on the costs of an efficient carrier.
>
> We also agree with the Joint Board that a forward-looking economic cost methodology is the best means for determining the level of universal service support. We find that a forward-looking economic cost methodology creates the incentive for carriers to operate efficiently and does not give carriers any incentive to inflate their costs or to refrain from efficient cost-cutting.

---

29 *See* Verizon Comments at p. 14.

> We note that California, Ohio, and Pennsylvania are using forward-looking economic cost studies for determining support levels in their intrastate universal service programs.
>
> As the Joint Board recognized, to the extent that it differs from forward-looking economic cost, embedded cost provide the wrong signals to potential entrants and existing carriers. The use of embedded cost would discourage prudent investment planning because carriers could receive support for inefficient as well as efficient investments. The Joint Board explained that when "embedded costs are above forward-looking costs, support of embedded costs would direct carriers to make inefficient investments that may not be financially viable when there is competitive entry."
>
> We also agree with CPI that the use of embedded cost to calculate universal service support would lead to subsidization of inefficient carriers at the expense of efficient carriers and could create disincentives for carriers to operate efficiently.[30]

In the 2001 *RTF Order*, the FCC recognized the difficulties the RTF had in developing a forward-looking cost model for rural carriers, but also noted that implementing a model could be done:

> As some commenters point out, the Rural Task Force's analysis of the forward-looking mechanism was based on the results of running the existing high-cost universal service model for rural companies using non-rural inputs. Because it found significant differences in comparing these results with actual company data, the Rural Task Force found that the model was not an appropriate tool for determining forward-looking costs of rural carriers. If inputs based on rural carrier data had been used, however, many of these differences could have been eliminated. Other differences identified by the Rural Task Force with respect to individual companies are generally the discrepancies one would expect when inputs designed for non-rural companies are used for an analysis of rural costs.
>
> The Commission has long recognized that the mechanism used to determine forward-looking cost for rural carriers may differ from that used for non-rural carriers. For instance, one could design a forward-looking mechanism for rural carriers that uses different benchmarks and averaging conventions.[31]

---

[30] 12 FCC Rcd at 8899-8901 (footnotes omitted).

[31] *Federal-State Joint Board on Universal Service, Fourteenth Report and Order, Twenty-second Order on Reconsideration, and Further Notice of Proposed Rulemaking*, 16 FCC Rcd 11244, 11312-11313 (2001) ("*RTF Order*") (footnotes omitted).

In the past three years, the Commission has not actively investigated how to implement a forward-looking cost model that contains rural inputs. No record evidence has been introduced that it cannot be done. There is every reason to believe a forward-looking cost model will be just as accurate, if not more so, than the current modified embedded cost model which permits the vast majority of average schedule carriers to submit no cost data on which support can be properly based. There are undoubtedly substantial inaccuracies and inefficiencies in the current system. Some have postulated that it would be expensive to reform the models developed in the RTF process. It is highly unlikely that the cost of making the forward-looking cost model work properly could be more than a small fraction of the funds being overspent today on the modified embedded cost methodology.

A forward-looking methodology will accomplish one critical objective – eliminating the incentive for ILECs to make inefficient investments in order to garner support. It is critical to note that consumers would be well served because today only CETCs have the proper incentive to invest efficiently. The per-line support mechanism requires CETCs to invest in an area based upon sound market-based principles. If a request for service cannot be accommodated because an investment will be inefficient, then the CETC commits to serve that customer through resale, and as such, forfeits support for that customer.

VIII. RESPONSES TO COMMENTS

We offer the following responses to comments filed on October 15.

CTIA, Nextel, and Western Wireless present sound proposals for transitioning rural ILECs to forward-looking costs.[32] RCA-ARC supports consideration of these commenters' proposals, simply because the use of forward-looking costs will promote efficient investment by

---

[32] *See* CTIA Comments at pp. 21-25; Nextel Comments at pp. 7-9; Western Wireless Comments at pp. 21-30.

incumbents and competitors.[33] The current modified embedded cost system provides excessive support to incumbents and promotes inefficient investment. Consumers in states that support rural America should not be over-subsidizing universal service. If it takes another Rural Task Force process to improve a forward-looking cost model or design a simple, transparent, technologically neutral, and unified means of distributing universal service in rural areas, then that project should commence at once so that reform can be implemented as close to June of 2006 as possible.

CenturyTel complains that "the population density in rural area is steadily declining, and there has been no indication that flight from rural areas to relatively urban areas will reverse itself any time soon."[34] One of the root causes of flight to urban areas is antiquated telecommunications infrastructure, which makes many rural areas less attractive to locate businesses that create jobs. The obvious answer to this problem is to promote universal service policies that will enable wireless carriers to accelerate infrastructure investment to improve coverage in rural communities, which will make many areas more desirable for businesses.

CenturyTel also notes that rural consumers have significantly less purchasing power than those in non-rural areas, noting that the median family income in rural areas is $41,102 compared to $54,657 in non-rural areas."[35] This statistic ignores the fact that rural consumers have a significantly lower cost of living and therefore generally pay less for goods and services

---

33 In affirming the FCC's forward-looking pricing model for leasing network elements, the Supreme Court noted, "the claim that TELRIC is unreasonable as a matter of law because it simulates but does not produce facilities-based competition founders on fact. The entrants have presented figures showing that they have invested in new facilities to the tune of $55 billion since the passage of the Act (through 2000)" *Verizon v. FCC*, 535 U.S. 467, 122 S.Ct. 1646, 1675 (2002).

34 CenturyTel Comments at p. 5.

35 *Id.*

than do their urban counterparts.[36] There is no shortage of persons living near or below the poverty line in our nation's urban areas, and they pay significantly more for basic wireline telecommunications services, including a federal universal service charge to subsidize their rural counterparts, including those who are wealthy.

CenturyTel improperly asks the Joint Board to look solely at the rates for local service, when the real inequities are in the amounts wireline consumers pay for toll calls. CenturyTel and other rural ILECs offer comparatively small local calling areas for basic service, advertising "unlimited" calling to only a few thousand, or even a few hundred other numbers. For many rural ILEC customers, every other call incurs toll. Meanwhile, high-cost support has enabled many RCA-ARC members to drive competitively priced rate plans into rural areas to provide consumers with the choices they are demanding. The Commission should consider whether rural areas that have very low basic telephone rates, sometimes below $10.00 per month, are being over-subsidized.[37] Moreover, when comparing pricing, the only true measure of affordability is the total amount, on average, that consumers pay for voice services. Today, wireless voice services are on par with wireline services, and wireless prices continue to drop.[38]

CenturyTel states that "[T]raditional wireline telecommunications carriers have for the first time in history suffered from a reduction in the total number of lines served and minutes of use per line."[39] As a result, "Rural carriers rely more heavily than non-rural carriers on access

---

36 According to the Economic Research Service of the United States Department of Agriculture, the cost of living in rural areas is about 16% lower than in urban areas. *See* Economic Research Service, Briefing Room: Rural Income, Poverty and Welfare at http://www.ers.usda.gov/Briefing/IncomePovertyWelfare/Overview.htm.

37 *Alenco*, *supra*, 201 F.3d at 620.

38 *See, e.g., Wireless Waxes While Wireline Wanes*, Telephony, November 8, 2004 at p. 22 (Household spending on wireless services comparable with wireline spending).

39 CenturyTel Comments at p. 11.

charges to assist in keeping rates affordable for their customers."[40] While it is true that wireless minutes of use and household spending have outstripped wireline usage and household spending, it is misleading to assert that access charges keep rates affordable. It may be more accurate to state that access charges keep *basic service* (*i.e.*, service that permits local calling to comparatively few other numbers) at artificially low, or even below-cost rates. Of course, the customer pays comparatively high prices for intra-state toll calls, some of which are only a few miles in distance, while every other user of the network must contribute to CenturyTel's rate structure by paying its access charges.

CenturyTel also emphasizes carrier of last resort ("COLR") as one of the "unique challenges" facing it and other rural ILECs.[41] Many ILECs claim that COLR obligations are a burden, yet in many states ILECs use COLR rules much to their advantage. The obligation to serve is not absolute in most states[42] and most often ILECs are permitted to levy a construction charge in their tariffs, which denies service to consumers unwilling to pay it. In some areas of the country, especially tribal lands, household telephone penetration levels are well below acceptable standards, in some cases below 50%. In some areas, ILECs have held orders[43] and have

40 *Id.* at p. 12.

41 *Id.* at pp. 7, 8, 9, 10, 12, 16. GVNW Consulting, Inc ("GVNW") even goes so far as to state that "one's view of equity is influenced primarily by whether one is an ILEC providing ubiquity or a CLEC meeting less stringent standards." GVNW Comments at p. 15. A more apposite phrasing would be that "one's view of equity is influenced primarily by whether one is a wireless CETC that is accustomed to competition and has the incentive to acquire and keep consumers along with the accompanying per-line high-cost support, or an ILEC that has allowed itself to become dependent on rate-of-return regulation and access to explicit and implicit subsidies."

42 *See Bluestem Tel. Co., et al. v. Kansas Corp. Comm'n,* (Ks. Dist. Ct. April 30, 2004) (appeal pending) ("...the COLR must show its costs for maintaining an infrastructure which may or may not provide actual services to citizens of the LEC's area.")

43 For example, on information and belief, ILECs have hundreds of held orders in rural New Mexico.

vigorously opposed state proposals to extend service to requesting consumers.[44] Wireless ETCs have a similar obligation to provide service upon reasonable request, and they must commit to step in and serve the entire area should the wireline carrier relinquish its ETC status.[45]

OPASTCO and GVNW, finding little to hang their hats on in the Act, appellate court decisions, and the FCC's orders, cite a state case to support the faulty proposition that "providing CETCs with the ILEC's cost-based support is not competitively neutral."[46] Both commenters fail to mention that the *Bluestem* decision of the Kansas District Court of Nemaha County is now on appeal before the Kansas Supreme Court. Moreover, *Bluestem* is inapposite because the case involved not the 1996 Act, but a state telecommunications statute which expressly provides that state universal service support for all carriers is to be calculated on the basis of each carrier's embedded costs. K.S.A. 66-2008(e). The case is not relevant to a determination of how *federal* universal service support should be distributed in light of the pro-competitive purposes of the 1996 Act. In addition, if it is affirmed by the Kansas Supreme Court, the fact that the law may violate the *Kansas Preemption Order* cited above makes it subject to possible federal preemption.

TCA estimates that 100% of lost federal support as a result of reform would have to be replaced by an increase in state support.[47] This presumes that ILECs actually need every dollar of

---

[44] ARC members are aware of such cases in Minnesota and Washington.

[45] *See, e.g., Western Wireless Corp., Petition for Designation as an Eligible Telecommunications Carrier in the State of Wyoming,* 16 FCC Rcd 48, 56 (2000) ("*Western Wireless*"), *recon. denied*, 16 FCC Rcd 19144 (2001); *Guam Cellular and Paging, Inc. d/b/a Guamcell Communications,* CC Docket No. 96-45, DA 02-174 (C.C.B. rel. Jan. 25, 2002) at ¶ 17 ("*Guamcell*"); *Western Wireless Corp., Petition for Designation as an Eligible Telecommunications Carrier for the Pine Ridge Reservation in South Dakota,* 16 FCC Rcd 18133, 18139 (2001) ("*Pine Ridge*").

[46] *See* OPASTCO Comments at p. 13; GVNW Comments at p. 15.

[47] TCA Comments at p. 7.

support they receive today. Yet TCA presents absolutely no analytical evidence that ILECs would be forced to increase their prices by the amount of federal support lost due to reform. In fact, the true revenue requirement for the vast majority of average schedule companies cannot be determined. A carrier may be able to increase operational efficiencies, seek out other sources of revenues, or in some cases, lower its dividend. Only by introducing incentives for all carriers to operate efficiently will fund growth be controlled.

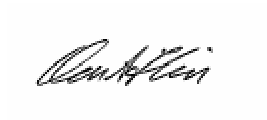
IX. CONCLUSION

In sum, RCA-ARC embraces many constructive ideas for managing growth of the fund while continuing a competitively neutral course that Congress set in 1996 and the FCC has faithfully carried out for eight years. Forward-looking costs would reduce support to all carriers in the long run. Proper disaggregation of support would reduce support to CETCs but not to ILECs. Forcing all carriers to compete for customers and support, with support levels meaningfully capped and made fully portable, will restrain fund growth while ensuring that consumers come first. To the contrary, rural ILEC interests have not offered any constructive proposal that is competitively and technologically neutral. They continue to advocate policies that presume that ILECs are the only “true” source of universal service, to the exclusion of all other technologies.

As the wireline business recedes over the next decade because people prefer wireless, this Commission must advance policies that encourage wireless carriers use high-cost funds to develop wireless infrastructure in rural areas. Proposals put forth by RCA-ARC, by CTIA, by Nextel, and by Western Wireless all advance the goals of the 1996 Act without asking for anything other than a level playing field with rural ILECs.

Respectfully submitted,

RURAL CELLULAR ASSOCIATION
THE ASSOCIATION OF RURAL CMRS CARRIERS



By: ______________________________________
David A. LaFuria
David L. Nace
Steven M. Chernoff

Lukas, Nace, Gutierrez & Sachs, Chartered
1650 Tysons Blvd., Suite 1500
McLean, VA 22102
703-584-8678

December 14, 2004